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IN THE

Supreme Court of the United States

OCTOBER TERM, 1944

NO. 23

E. JACK SMITH, JACK CLARK, R. L. RIVERS, and W. CORRY SMITH, partners trading under the firm name of E. JACK SMITH, CONTRACTOR,

Petitioners,

vs.

COMER DAVIS, REESE PERRY and JOHN C. TOWNLEY, as board of county tax assessors of Fulton County, et al.,

Respondents.

BRIEF ON BEHALF OF PETITIONERS

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SUBJECT INDEX

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Reference to Report of Opinions In Courts Below

The opinion of the Supreme Court of Georgia is printed in 28 S.E. 2nd. 148 (Advance Sheet No. 2, January 20, 1944).

STATEMENT OF JURISDICTION

The jurisdiction of this Court is invoked under Section 237(b) of the Judicial Code as amended by the Act of February 13, 1925 (28 U.S.C.A. §344), in that petitioners in their original action brought in the Superior

Court of Fulton County, being the court of first instance, specially set up and claimed in their equitable bill filed therein a title, right, privilege and immunity under the Constitution of the United States (R. 5), which Federal claim was expressly denied to them by the decision and judgment of the Supreme Court of Georgia entered on the 11th day of November, 1943 (R. 55, 68). This was a final judgment or decree rendered by the highest court of the State in which a decision could be had. (R. 68.) This Court granted the writ of certiorari on April 3, 1944.

STATEMENT OF THE CASE

Petitioners, as partners, were engaged in the contracting and construction business and as such had furnished paving materials and done work in constructing public highways for the State of Georgia and various counties of the State and in building United States Army air bases for the United States of America. For work so done, the State of Georgia, the County of Camden, and the United States Government owed petitioners on January 1, 1942, various sums. At that time the debt of the State was evidenced by a certificate of indebtedness amounting to $117,050.00, in addition to an open account of $15,086.84, while the obligations due by Camden County and the United States to petitioners took the form of open accounts. The former stood at $1,102.14, the latter at $29,831.10.

In the fall of 1942, the partners, now petitioners here, brought their equitable bill in the Superior Court of Fulton County against named county tax officials, respondents here, seeking thereby to enjoin them from assessing

against petitioners, as property subject to State and County ad valorem taxation, the accounts and certificates owned to them on the first day of the year by the Federal Government, the State and the County. The bill challenged the right to make the assessment which was threatened upon the ground that such assessment was prohibited both by the due process clauses of the State and National Constitutions. Furthermore, petitioners' bill denied the right of the defendants to carry out their avowed purpose of taxing these accounts and certificates because to do so would be to impose a state and county tax upon instrumentalities of the United States of America, the State of Georgia, and a governmental subdivision of the State, in contravention of constitutional limitations of the Federal and State Constitutions.

Against the petition as twice amended the defendants lodged a general demurrer through which the petition's dismissal was sought upon the ground that it appeared affirmatively from the allegations as made therein that "each species of property owned by petitioners," i. e., the accounts and the certificates, was taxable property, owned on January 1, 1942, by petitioners and as such was subject to tax in and by Fulton County and the State of Georgia. The trial court overruled the demurrer, but the Supreme Court of Georgia, to which the losing tax officials took the case by exceptions, reversed and, with one Justice dissenting, entered a judgment on November 11, 1943, directing that the general demurrer be sustained and the petition dismissed. The issue of constitutional immunity from local taxation of open accounts when owed by the Federal Government was squarely

raised in the State Supreme Court and there as squarely decided (R. 55).

QUESTIONS PRESENTED

1. Whether an open account owed by the United States of America for construction work done for it is such an instrumentality or means of the Federal government as to be immune from ad valorem taxes which the State may lay upon personal property (defined by statute to include money due on open accounts) otherwise taxable by it.

2. Whether the implied constitutional limitation on the power of the State to tax the functions, activities and instrumentalities of the National Government extends to and includes within the prohibition an account due and owing by the United States to a contractor for construction work done by him for it.

3. Whether an account due and owing by the United States Government to a contractor for work done and material furnished by him to it is such an instrumentality or means of the Federal government that it cannot be taxed by State or local government.

STATUTES INVOLVED

Georgia Code 1933, Section 92-101 provides: "All real and personal property, whether owned by individuals or corporations, resident or nonresident, shall be liable to taxation, except as otherwise provided by law."

Georgia Code 1933, Section 92-102 provides: "For the purposes of taxation, 'personal property' shall be construed to include goods, chattels, moneys, credits and

effects, whatsoever they may be; ships, boats, and vessels, whether at home or abroad, and capital invested therein; bonds and other securities of corporations of this or of other States; stock of corporations of other States; bonds, notes or other obligations of other States, and of the counties, municipalities or other subdivisions thereof; money due on open account or evidenced by notes, contracts, bonds, or other obligations, secured or unsecured."

SPECIFICATION OF ERROR

The Supreme Court of Georgia erred:

1. In reversing the judgment of the trial court.

2. In holding that an account receivable due from the United States to a contractor is taxable as property in the hands of the contractor.

3. In applying the reasoning of the court and the conclusions reached in the cases of *James v. Dravo Contracting Company*, 302 U. S., 134, and *Penn Dairies v. Milk Control Commissioner*, 318 U. S., 261, to a case which involved a tax sought to be imposed upon an instrumentality, means and operation whereby the United States exercises its governmental powers rather than upon a contractor as an agent or instrument of the government.

4. In failing to hold that an open account owing by the United States is an instrumentality or means of the National Government within the meaning of the taxing prohibition announced in *McCulloch v. Maryland*, 4 Wheat., 316; *Weston v. Charleston*, 2 Pet., 449; and *The Banks v. The Mayor*, 7 Wall., 16.

As will be noted in the Georgia statutes previously quoted, personal property is liable to ad valorem taxation in Georgia. Such property "includes * * credits and effects, whatsoever they may be; * * money due on open account or evidenced by notes, contracts, bonds or other obligations, secured or unsecured." Consequently, respondents would have been acting with ample statutory support in assessing for taxes against petitioners the moneys due them from the United States upon open account were it not for the restraint imposed by the doctrine that State and local governments are not free to tax instrumentalities of the Federal government. The majority opinion in the court below, while recognizing the rule, holds that it is without application to an ad valorem tax laid upon an open account. In effect Georgia's Supreme Court decides that an account owing to the United States for material and labor furnished to it under contract is not an instrumentality or means of the National Government within the meaning of the taxing prohibition that was stated in, and has stood since, the decision in *McCulloch v. Maryland*, supra. Petitioners here question that view and seek here a judgment which would follow the law announced in the dissenting opinion in the State court.

DIVERGENT VIEWS

The essence of the question that is now presented to this Court is whether the facts of the instant case are to be ruled by such cases as *McCulloch v. Maryland*, supra, *The Banks v. The Mayor*, supra, *Weston v. Charleston*,

supra, and *Indian Motorcycle Co. v. U. S.*, 283 U. S., 570, or by such decisions as *James v. Dravo Contracting Company*, supra, *Alabama v. King & Boozer*, 314 U. S., 1, and *Penn Dairies v. Milk Control Commission*, supra. We think that it is the doctrine of the former and not of the latter cases that should govern.

CONTRACTOR AS AGENT OR INSTRUMENTALITY OF GOVERNMENT NOT HERE INVOLVED

At the base of the decisions in the *Dravo, King & Boozer*, and *Penn Dairies* cases is the holding that the contractor who does work for the Federal Government is not on that account an agent or instrumentality of the Government. Thus in the *Dravo* case a non-discriminating State tax laid upon the gross receipts of an independent contractor received under his contract with the United States was sustained over the contention that the contractor was himself an instrument of government and that the tax was laid upon the contract itself. In the case of *King & Boozer*, a sales tax of Alabama was upheld when applied to purchases of materials made by a contractor when bought for use, and used, in the performance of a "cost plus" building contract for the government. The basic holding was that such a contractor was not the agent of the government in making the purchases and in consequence the tax was not laid upon the government as the buyer. The Court in the *Penn Dairies* case repeated its earlier holding that those who furnish supplies and render services under contract to the government are not Federal agencies, are not immune from non-discriminatory State taxes, and are subject to State regulation, including price fixing.

Distinguishing the rulings made in those cases, of which *James v. Dravo Contracting Company*, supra, is typical, this Court in *United States of America v. County of Allegheny*, 88 L. ed. 845 (U. S. Supreme Court Law. ed. Advance Opinions No. 14) said:

> "But in all of these cases what we have denied is immunity for the contractor's own property, profits, or purchases. We have not held either that the Government could be taxed or its contractors taxed because property of the Government was in their hands. The distinction between taxation of private interests and taxation of governmental interests, although sometimes difficult to define, is fundamental in application of the immunity doctrine as developed in this country."

Tax immunity in the present case is not grounded upon the consideration that the contractor, whose debt from the government was in the form of an account receivable, was because of that circumstance an agent of the United States. Nor is tax exemption sought because the account represents work done for and material furnished to the government. Petitioners here ask this Court to view the tax which the Georgia Supreme Court has validated as one to be imposed directly upon an instrumentality, means and an operation whereby the United States exercises its governmental powers. So seen, the tax must fall, on the authority of cases reaching from *McCulloch v. Maryland*, supra, to *United States v. County of Allegheny*, supra, where the holding has been that the supremacy clause of the Federal Constitution proscribes any state tax which impedes the functions of the National Government.

PRINCIPLE OF TAX IMMUNITY ABSOLUTE

The doctrine of tax immunity does not depend upon the degree of interference but rests upon the entire absence of power on the part of the state to tax instrumentalities of the United States.

This Court said in *Johnson v. Maryland*, 254 U. S. 51 at page 55:

> "With regard to taxation, no matter how reasonable, or how universal and undiscriminating, the state's inability to interfere has been regarded as established since *McCulloch v. Maryland*, 4 Wheat., 316, 4 L. ed. 579, and that is the law today. The decision in that case was not put upon any consideration of degree, but upon the entire absence of power on the part of the states to touch, in that way at least, the instrumentalities of the United States."

In the same connection, this Court said, in *Indian Motorcycle Co. v. U. S.*, supra, at page 575:

> "It is an established principle of our constitutional system of dual government that the instrumentalities, means and operations whereby the United States exercises its governmental powers are exempt from taxation by the States, and that the instrumentalities, means and operations whereby the States exert the governmental powers belonging to them are equally exempt from taxation by the United States. This principle is implied from the independence of the national and state governments within their respective spheres and from the provisions of the Constitution which look to the maintenance of the dual system. * * Where the principle applies it is not affected by the amount of the particular tax or the extent of the resulting interference, but is absolute."

THE OBLIGATION OF THE UNITED STATES RESTING IN OPEN ACCOUNT IS AN INSTRUMENTALITY OF THE GOVERNMENT.

The question, then, narrows itself to a determination of whether the obligation of the United States to a contractor represented by an open account made up of items for material and labor furnished under a contract (R. 32) for the construction of an air base is an instrumentality and means of the government used in carrying on its civil and military operations. If it is, then the State of Georgia and its subdivision, the County of Fulton, are powerless to subject it to taxation. If it is not, the proposal of local state and county officials to tax it must be, as it was, upheld.

In the first place, it may be noticed that the contract (R. 32) between petitioners and the War Department of the United States of America from which the obligation arises is one forming a part of the vast program upon which the nation has embarked in its effort to carry the war to victory. The governmental powers involved, therefore, include the war making power of the Congress in addition to those others vested by the Constitution in the Government of the United States (Constitution, Art. I, §8). This Court may well take judicial cognizance of the fact that in providing the many, expensive and diverse facilities requisite to the training, and equipping of the country's armed forces, the departments and agencies of the government have relied heavily, if not entirely, upon the national credit. A common form in which this credit appears is of money due by the United States to contractors under construction contracts. In

other words, the government's operations in the vast fields of training, equipping, feeding, housing and transporting our armed forces are dependent in no small way upon government credit which has taken the form of debts due under contract, i.e., open accounts with various contractors.

But apart from the extensive use of open account credit by the government in the furtherance of the war effort, it must be plain that this type of credit is utilized constantly by the United States, and its agencies. It is a means universally employed to obtain credit, and in many instances it is as effectual as written evidence of the obligation, such as notes, debentures or certificates of indebtedness.

A debt owed by the government, then, whatever form it may take, is an obligation of the government, and a tax upon it is a tax upon the credit of the government. In pointing out the distinction between a State tax upon federal checks and warrants and one upon governmental obligations, this Court said in *Hibernia Savings Society v. San Francisco*, 200 U. S. 310, 313:

> "The basis of this exemption is the fact that a tax upon the obligations of the United States is virtually a tax upon the credit of the Government, and upon its power to raise money for the purpose of carrying on its civil and military operations. The efficiency of the Government service cannot be impaired by a taxation of the agencies which it employs for such service, and, as one of the most valuable and best known of these agencies is the borrowing of money, a tax which diminishes in the slightest degree the

value of the obligations issued by the Government for that purpose impairs pro tanto their market value."

McCulloch v. Maryland established the doctrine that obligations of the United States issued by it as a means of providing revenue, or for the payment of its debts, were beyond the reach of taxation by the States. The Chief Justice repeated the doctrine in *Weston v. City Council of Charleston*, supra, and the Court there, invalidating local taxes on what was then called "stock" of the United States, owned by an individual, held such a tax to be one laid upon the power to borrow money on the credit of the United States, and hence unconstitutional. Speaking for the Court, Chief Justice Marshall said (at p. 468):

"The right to tax the contract to any extent, when made, must operate upon the power to borrow before it is exercised, and have a sensible influence on the contract. The extent of this influence depends on the will of a distinct government. To any extent, however inconsiderable, it is a burden on the operation of government. It may be carried to an extent which shall arrest them entirely."

It remained for the Court to apply this rule to obligations of the government incurred, not for money borrowed upon government credit, but for supplies and materials furnished to it and for which it had issued its certificates of indebtedness. This application was made in *The Banks v. The Mayor*, supra, where it was said:

"Evidences of indebtedness of the United States * * sometimes called stock or stocks, but recently

better known as bonds or obligations, have uniformly been held by this court not to be liable to taxation under State legislation * * . No one affirms that the power of the government to borrow, or the action of the government in borrowing, is subject to taxation by the States. * * An attempt was made * * to establish a distinction between the bonds of the government expressed for loans of money and the certificates of indebtedness for which the exemption was claimed. The argument was ingenious, but failed to convince us that such a distinction can be maintained. It may be admitted that these certificates were issued in payment of supplies and in satisfaction of demands of public creditors. But we fail to perceive either that there is a solid distinction between certificates of indebtedness issued for money borrowed and given to creditors, and certificates of indebtedness issued directly in payment of their demands; or that such certificates, issued as a means of executing constitutional powers of the government other than borrowing money, are not as much beyond control and limitation by the States through taxation, as bonds or other obligations issued for loans of money. * * The certificates of indebtedness * * were received instead of money at a time when full money payment for supplies was impossible, and * * are as much beyond the taxing power of the States, as the operations themselves in furtherance of which they were issued."

So far as we have been able to find, a single court, only, has passed upon the precise point which the present petition raises. In *People ex rel. Astoria Light, Heat & Power Co. v. Cantor*, 143 N. E. 901, the New York Court of Appeals was asked to hold that an amount due from the United States for the manufacturing and furnishing of

gas masks during the last war was simply an indebtedness due from a solvent debtor and was ordinary personal property, assessable and taxable by the State. That Court, in refusing to accept such a view and, upon the authority of the cases which we have just discussed and upon the principles laid down in them, said:

> "We do not agree with this view. We think that the power of a state to tax the amounts becoming due under a contract with the Federal Government like the one in question would hinder and embarrass the government in carrying out the powers conferred by the constitutional provisions above quoted. If we should assume that a state, carried away by some species of popular passion or some fatuous theory of federal and state relations, should enact a law providing that the amount coming due to one of its citizens from the federal government under such a contract as this should be taxed at 50 per cent. of its amount, we think no one could doubt that the federal government would be hindered and embarrassed by such action in making contracts to enable it to carry on war. It either would not be able to get persons to take such contracts, or it would be compelled to add to the amount of compensation to be paid to them the extra amount which the state proposed to take by way of taxation. Either result would be a handicap and a source of hinderance; and in our judgment would clearly come within the abiding principles laid down in *McCulloch v. Maryland*, 4 Wheat. 316, 4 L. ed. 579, and *The Banks v. New York*, 7 Wall. 16, 19; L. ed. 57. The fact that the tax might be 2 per cent. instead of 50 per cent. would alter the amount of embarrassment but not the principle involved."

The dissent in the court below characterized this New

York case "as the necessary sequence" of what this Court said in *The Banks v. The Mayor*. And so it seems to us.

CONCLUSION

We say, with the dissenting Justice of the State Court, that the Federal "instrumentality" which the State may not tax is not a word having a special, narrow significance. It denotes the means by which the governmental activity is conducted. It embraces notes as an instrumentality for borrowing money and obtaining credit; certificates of indebtedness as a means of obtaining supplies and materials upon credit. It must, so it seems to us, include an open account when used as a medium by which the government gets work done and material furnished. Both the certificate of indebtedness and the open account are means used for the same end, and that end is credit. If the tax locally laid upon the certificate is invalid for the reasons stated in *The Banks v. The Mayor*, the tax sought to be imposed upon the open account in the instant case is also invalid, and for the same reasons.

Respectfully submitted,

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